

Washington State Auditor's Office

Audit Report

Audit Services

Report No. 57795

PIERCE COUNTY HOUSING AUTHORITY

Pierce County, Washington

July 1, 1994 Through June 30, 1995

Issue Date: October 18, 1996

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PIERCE COUNTY HOUSING AUTHORITY
Pierce County, Washington
July 1, 1994 Through June 30, 1995

Background

During our audit, the housing authority's executive director, chief financial officer, and controller (all management staff responsible for and knowledgeable about the financial statements accompanying this report) resigned. As a result, we were unable to obtain a letter, required by auditing standards, in which management makes written representations concerning the availability of all records, related party disclosures, unrecorded transactions, and compliance with laws and regulations, among other things.

Further, during our examination of the housing authority's financial records, we found pervasive weaknesses in its internal control structure, accounting system, and ability to prepare accurate and complete financial statements.

We also must point out that the housing authority's Enterprise Fund has suffered recurring losses from operations, has a net capital deficiency, and has substantial debt payments on three loans due October 1 and December 1, 1996. To meet these debt payments, the housing authority is seeking to extend or refinance the loans, the terms of which depend on appraisals of the secured properties. As the appraisals have not yet been made, the housing authority's ability to meet the debt payments is not known.

Housing authority officials are working to correct these financial deficiencies. We remain committed to assisting the agency in any way we can to restore its financial health.

PIERCE COUNTY HOUSING AUTHORITY
Pierce County, Washington
July 1, 1994 Through June 30, 1995

**Independent Auditor's Report On Compliance With Laws And Regulations
At The Financial Statement Level (Plus Additional State Compliance
Requirements Per RCW 43.09.260)**

Board of Commissioners
Pierce County Housing Authority
Tacoma, Washington

We have audited the general-purpose financial statements, as listed in the table of contents, of the Pierce County Housing Authority, Pierce County, Washington, as of and for the fiscal year ended June 30, 1995, and have issued our report thereon dated July 12, 1996.

Our report was modified because the housing authority was unable to provide written representations that generally accepted auditing standards require us to obtain and because the financial statements contain several departures from generally accepted accounting principles.

Except as discussed in the following paragraph, we conducted our audit in accordance with generally accepted auditing standards and *Government Auditing Standards*, issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement.

Because of the resignations of the housing authority's executive director, chief financial officer, and controller, we were unable to obtain written representations from the authority's management that generally accepted auditing standards require us to obtain.

Compliance with laws, regulations, contracts, and grants applicable to the Pierce County Housing Authority is the responsibility of the housing authority's management. As part of obtaining reasonable assurance about whether the financial statements are free of material misstatement, we performed tests of the housing authority's compliance with certain provisions of laws, regulations, contracts, and grants.

We also performed additional tests of compliance with state laws and regulations as required by *Revised Code of Washington (RCW) 43.09.260*. This statute requires the State Auditor to inquire as to whether the housing authority complied with the laws and the *Constitution of the State of Washington*, its own ordinances and orders, and the requirements of the State Auditor's Office. Our responsibility is to examine, on a test basis, evidence about the housing authority's compliance with those requirements and to make a reasonable effort to identify any instances of misfeasance, malfeasance, or nonfeasance in office on the part of any public officer or employee and to report any such instance to the management of the housing authority and to the Attorney General. However, the objective of our audit of the financial statements was not to provide an opinion on overall compliance with these provisions. Accordingly, we do not express such an opinion.

Material instances of noncompliance are (1) failures to follow requirements or violations of prohibitions contained in statutes, regulations, contracts, or grants that cause us to conclude that the aggregation of the misstatements resulting from those failures or violations is material to the financial statements or (2) considerable failure to comply with the laws and the *Constitution of the State of Washington*, the housing authority's ordinances and orders, and the requirements of the State Auditor's Office. The results of our tests of compliance disclosed instances of noncompliance that may materially affect the financial statements, the effects of which have been corrected in the housing authority's financial statements. The material instances of noncompliance noted during our audit are disclosed in the accompanying Schedule of Findings.

We considered the instances of noncompliance in forming our opinion on whether the housing authority's financial statements are fairly presented, in all material respects, in conformity with generally accepted accounting principles and the statutory provisions described in paragraph four of this report. This report does not affect our report dated July 12, 1996, on those financial statements.

Except for the material instances of noncompliance disclosed in the Schedule of Findings accompanying this report, the results of our tests of compliance indicate that, with respect to the items tested, the housing authority complied, in all material respects, with the provisions referred to in the third and fourth paragraphs of this report, and with respect to items not tested, nothing came to our attention that caused us to believe that the housing authority had not complied, in all material respects, with those provisions.

We also noted matters involving noncompliance with laws and regulations related to federal financial assistance which were reported to the housing authority's management in our reports on general requirements and specific requirements for major programs.

This report is intended for the information of management, officials of HUD, and the board of commissioners and to meet our statutory reporting obligations. This report is a matter of public record and its distribution is not limited. It also serves to disseminate information to the public as a reporting tool to help citizens assess government operations.

Brian Sonntag
State Auditor

July 12, 1996

PIERCE COUNTY HOUSING AUTHORITY
Pierce County, Washington
July 1, 1994 Through June 30, 1995

Independent Auditor's Report On Internal Control Structure
At The Financial Statement Level

Board of Commissioners
Pierce County Housing Authority
Tacoma, Washington

We have audited the general-purpose financial statements of the Pierce County Housing Authority, Pierce County, Washington, as of and for the fiscal year ended June 30, 1995, and have issued our report thereon dated July 12, 1996.

Our report was modified because the housing authority was unable to provide written representations that generally accepted auditing standards require us to obtain and because the financial statements contain several departures from generally accepted accounting principles.

Except as discussed in the following paragraph, we conducted our audit in accordance with generally accepted auditing standards and *Government Auditing Standards*, issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement.

Because of the resignations of the housing authority's executive director, chief financial officer, and controller, we were unable to obtain written representations from the authority's management that generally accepted auditing standards require us to obtain.

The management of the housing authority is responsible for establishing and maintaining an internal control structure. In fulfilling this responsibility, estimates and judgments by management are required to assess the expected benefits and related costs of internal control structure policies and procedures. The objectives of an internal control structure are to provide management with reasonable, but not absolute, assurance that assets are safeguarded against loss from unauthorized use or disposition, and that transactions are executed in accordance with management's authorization and recorded properly to permit the preparation of financial statements in accordance with generally accepted accounting principles. Because of inherent limitations in any internal control structure, errors or irregularities may nevertheless occur and not be detected. Also, projection of any evaluation of the structure to future periods is subject to the risk that procedures may become inadequate because of changes in conditions or that the effectiveness of the design and operation of policies and procedures may deteriorate.

In planning and performing our audit of the financial statements of the housing authority, we obtained an understanding of the internal control structure. With respect to the internal control structure, we obtained an understanding of the design of relevant policies and procedures and whether they have been placed in operation, and we assessed control risk in order to determine our auditing procedures for the

purpose of expressing our opinion on the financial statements and not to provide an opinion on the internal control structure. Accordingly, we do not express such an opinion.

We noted certain matters involving the internal control structure and its operation that we consider to be reportable conditions under standards established by the American Institute of Certified Public Accountants. Reportable conditions involve matters coming to our attention relating to significant deficiencies in the design or operation of the internal control structure that, in our judgment, could adversely affect the entity's ability to record, process, summarize, and report financial data consistent with the assertions of management in the financial statements.

The matters involving the internal control structure and its operation that we consider to be reportable conditions are included in the Schedule of Findings accompanying this report.

A material weakness is a reportable condition in which the design or operation of one or more of the specific internal control structure elements does not reduce to a relatively low level the risk that errors or irregularities in amounts that would be material in relation to the financial statements being audited may occur and not be detected within a timely period by employees in the normal course of performing their assigned functions.

Our consideration of the internal control structure would not necessarily disclose all matters in the internal control structure that might be reportable conditions and, accordingly, would not necessarily disclose all reportable conditions that are also considered to be material weaknesses as defined above. However, we noted a reportable condition that we believe to be a material weakness, which is identified in the Schedule of Findings accompanying this report.

We also noted matters involving compliance with laws and regulations related to federal financial assistance which were reported to the housing authority's management in our reports on general requirements and specific requirements for major programs.

This report is intended for the information of management, officials of HUD, and the board of commissioners and to meet our statutory reporting obligations. This report is a matter of public record and its distribution is not limited. It also serves to disseminate information to the public as a reporting tool to help citizens assess government operations.

Brian Sonntag
State Auditor

July 12, 1996

PIERCE COUNTY HOUSING AUTHORITY
Pierce County, Washington
July 1, 1994 Through June 30, 1995

Schedule Of Findings

1. The Housing Authority Should Prepare Accurate Financial Reports And Improve General Ledger Internal Controls

The Pierce County Housing Authority financial reports for fiscal year 1995 contained numerous errors. The errors were the result of inaccurate data accumulated in the accounting system due to material weaknesses in accounting controls and significant turnover of accounting staff. The inaccuracies included transactions posted to wrong funds and in incorrect amounts. The weak controls are discussed throughout the findings in this report and primarily include:

- a. The current general ledger system cannot be closed out, thus allowing transactions to be posted to the incorrect fiscal period.
- b. The general ledger was a 'moving' target which changed at least four times during the course of the audit.
- c. General ledger journal entries were prepared by management personnel without review or approval prior to entry into the general ledger system.
- d. Internal audit adjustments had no supporting documentation.
- e. Lack of closing review performed on the monthly Housing Assistance Payments failed to detect prior year Housing Assistance Payment data merged with current year data in the general ledger system, resulting in the processing of incorrect checks to landlords.
- f. No computer controls prevented transaction posting dates from differing from the actual calendar date of posting.

This finding has been continually repeated since 1991.

Both federal and state directives require accurate financial reports. The United States Department of Housing and Urban Development (HUD) Handbook 7420.7, Chapter 12-3 states in part:

Public Housing Authorities are required to maintain complete and accurate books of accounts and records for each program under the Annual Contributions contract. The books and records must comply with HUD requirements and must permit a speedy and effective audit.

RCW 43.09.230 states in part:

The state auditor shall require from every local government financial reports covering the full period of each fiscal year, in accordance with the forms and methods prescribed by the state auditor, which shall be uniform for all accounts of the same class.

Due to the deficiencies of the housing authority's internal control structure, its accounting system, and its inability to prepare accurate and complete financial statements, we have concluded the housing authority has significant and pervasive control problems.

We recommend housing authority officials take immediate action to correct the above noted weaknesses to enable the establishment and maintenance of current, accurate, and complete accounting records and that management review these records in a timely manner.

Auditee's Response

The Housing Authority has taken steps to solve the deficiency in the General Ledger System, including the creation of a new General Ledger File on the computer each year so that an errant key stroke will not allow the General ledger file to be updated incorrectly. The Authority has now required the General ledger journal entries to have a second signature before they are entered into the system, this is also true of any adjusting journal entries.

2. The Housing Authority Should Strengthen Internal Controls Over Purchases

During our testing of construction for the various apartment complexes managed by the housing authority, we noted duplicate billings for carpet and vinyl replacements. Further, units receiving carpeting and vinyl one month might have it replaced one or two months later.

The housing authority's primary internal control over purchasing is approval of purchase orders by a department supervisor. This assumes the supervisor knows whether the purchase is necessary. Because the maintenance department supervisors do not track repairs by unit, they would not know whether a purchase order is accurate or necessary. They also would not know whether an invoice for a particular unit had been doubled billed or whether replacements by unit appeared excessive.

The maintenance department supervisors believed the finance department was tracking such information. The finance department believed tracking was the maintenance department's responsibility. If the purchase order was approved, finance considered the expenditure legitimate and processed it for payment when the invoice was received.

RCW 42.24.080 states in part:

All claims presented . . . by persons furnishing materials, rendering services or performing labor . . . shall be audited, before payment, by an auditing officer . . . of the municipal corporation or political subdivision . . . The form shall provide for the authentication and certification by such auditing officer that the materials have been furnished, the services rendered or the labor performed as described, and that the claim is a just, due and unpaid obligation against the municipal corporation . . . and no claim shall be paid without such authentication and certification . . .

When internal controls over purchasing are weak, the risk increases that errors or irregularities could go undetected for some time. Inaccurate data on the purchase orders (such as unit identification) could lead to the unnecessary replacements and duplications. In addition, such weaknesses in the internal controls impair the ability to prepare accurate and timely financial information.

We recommend housing authority officials track major repairs and purchases by unit and review such information when considering the approval of purchase orders.

Auditee's Response

The Authority tracks purchases by apartment complex and by budget category. Currently the computer system is not capable of tracking by particular unit. Hand tracking each unit by category would be a tremendous task given the system now in place. The maintenance supervisor now has to sign off for major items to be replaced in a unit. This provided for the management control necessary to ensure no duplication of expenses occur.

3. The Housing Authority Should Strengthen Controls Over Executive Director's Expense Reimbursements

The former executive director's expense reimbursements were not adequately reviewed or approved.

We found no review or approval for 8 (\$5,243.84) of the former executive director's 18 reimbursement requests for fiscal year 1995. The other 10 reimbursement requests were approved by the former chief financial officer who worked for the director.

The housing authority's internal travel and expense policy does not address approval or review of the executive director's expense reimbursements.

We found that on four occasions during fiscal year 1995, the former executive director extended his stay for his own convenience while attending work-related out-of-state conferences. He requested and received reimbursement for all lodging, meals, parking, and other miscellaneous expenses related to these trip extensions. These reimbursements totaled \$823.86. In three of the four instances (\$556.43), the requests for reimbursement were not reviewed or approved.

RCW 42.24.090 states in part:

No claim for reimbursement of any expenditures by officers or employees of any municipal corporation or political subdivision of the state for transportation, lodging, meals or any other purpose shall be allowed by any officer, employee or board charged with auditing accounts unless the same shall be presented in a detailed account . . . All claims . . . shall be duly certified by the officer or employee submitting such claims on forms and in the manner prescribed by the state auditor.

The housing authority's internal policy, no. 200-01, 'Travel and Expense Policy', Section 5 (D)(e) states:

No reimbursement for lodging or subsistence or travel shall be paid to an employee for time away from his/her official station or residence incurred traveling to a destination for his own convenience in advance of a

reasonable time for arrival nor shall he/she be paid for extra time incurred if he/she remains at the destination following an official meeting other than a work assignment whenever it is for his/her own convenience.

The former executive director stated that by extending his stay over weekends, he was able to purchase less expensive airfare. However, no documentation exists to support his statement or to prove the amount of saved airfare exceeded the additional lodging and subsistence expenses.

We recommend the board of commissioners consider seeking reimbursement for these expenses. We also recommend the housing authority's travel policy be amended to require board of commissioners' approval of the executive director's expense reimbursements. We further recommend out-of-state travel extensions (if allowed) be preapproved and supported by appropriate documentation demonstrating the cost savings to the housing authority.

Auditee's Response

The auditor's request will be forwarded to the Board of Commissioners for their consideration and probable action.

4. Vacancy Reports Should Be Accurate

Our tests of the vacancy reports for several apartment complexes managed by the housing authority revealed at least one complex, Chateau Rainier, was not properly reporting and recording vacancy information.

Apartment complex managers prepare weekly vacancy reports which are used by the board of commissioners to monitor how well the housing authority is managing its properties. We compared the vacancy reports for January 1996 to the Rent Roll Report generated by the finance department based upon rental income received. The vacancy report for Chateau Rainier showed 11 units vacant, the Rent Roll Report showed 14. We determined the discrepancy was because the apartment manager does not list a unit as vacant if a future renter is known. A future renter may not occupy the unit for some time.

As a result, the board is relying upon misleading information.

We recommend apartment complexes managers consistently report actual vacancies on the weekly vacancy reports to provide accurate information to housing authority management and the board of commissioners.

Auditee's Response

The reports regarding vacancies at the apartment complexes were compared by the auditors to the rent roles that were provided for the finance office. The two reports are used for different purposes and should not be compared to each other for matching information. The reports at the complexes show the units which are available to prospective renters and allows the managers at the complex to track those units. The rent roles show the actual economic vacancies when no money is received for that particular month. It would be appropriate to explain the difference to the Board of Commissioners should the information be provided to them in one format or another. However, the inclusion of this as a finding should be reconsidered as the reports have no relevance to the accuracy of the financial reports.

Auditor's Concluding Remarks

We agree the vacancy reports are not relevant to the accuracy of the housing authority's financial statements. Such information is, however, relevant to the housing authority's financial condition. Concerns were expressed to us that the board was being provided inaccurate vacancy information. While our tests were inconclusive as to any deliberate falsification, we did note certain inaccuracies as reported herein. We therefore reaffirm our finding.

Based upon the response, the issues delineated in our report appear to have been addressed. We will review these areas again in our subsequent audit.

We would like to express our appreciation to staff for their assistance and cooperation throughout the audit process.

PIERCE COUNTY HOUSING AUTHORITY
Pierce County, Washington
July 1, 1994 Through June 30, 1995

**Independent Auditor's Report On Financial Statements And Supplemental
Information Required By HUD**

Board of Commissioners
Pierce County Housing Authority
Tacoma, Washington

We have audited the accompanying general-purpose financial statements of the Pierce County Housing Authority, Pierce County, Washington, as of and for the fiscal year ended June 30, 1995, as listed in the table of contents. These financial statements are the responsibility of the housing authority's management. Our responsibility is to express an opinion on these financial statements based on our audit.

Except as discussed in the following paragraph, we conducted our audit in accordance with generally accepted auditing standards and *Government Auditing Standards*, issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatements. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinion.

Because of the resignations of the housing authority's executive director, chief financial officer, and Controller, we were unable to obtain written representations from the authority's management that generally accepted auditing standards require us to obtain.

As described in Note 1 to the financial statements, the housing authority recognizes interest and principal on general long-term indebtedness when due and has not utilized a debt service fund to account for resources that will be used to service the general long-term debt recorded in the housing authority's General Long-Term Account Group. In our opinion, generally accepted accounting principles require the recognition of principle and interest when paid and the utilization of a debt service fund.

As also described in Note 1, the housing authority recognizes compensated absences related to its governmental funds when due. In our opinion, generally accepted accounting principles require such compensated absences be recorded in the housing authority's General Long-Term Account Group when future payments for such absences have been earned by employees.

In our opinion, except for the effects of such noncompliance, if any, as might have been determined to be necessary had we been able to obtain written representations from management, and except for the effects of not recognizing principal and interest when paid rather than due, omitting a debt service fund, and not recording compensated absences.

The financial statements referred to above present fairly, in all material respects, the financial position of the Pierce County Housing Authority, at June 30, 1995, and the results of its operations and cash flows of its proprietary fund types for the fiscal year then ended, in conformity with generally accepted accounting principles.

The housing authority's enterprise fund has suffered recurring losses from operations, has a net capital deficiency, and has substantial debt payments on three loans due October 1 and December 1, 1996. To meet these debt payments, the housing authority is seeking to extend or refinance the loans, the terms of which depend on appraisals of the secured properties. As the appraisals have not yet been made, the housing authority's ability to meet the debt payments is not known. The ultimate outcome of this situation cannot presently be determined. Accordingly, no provision for the outcome has been made in the accompanying financial statements.

Our audit was made for the purpose of forming an opinion on the financial statements taken as a whole. The accompanying Actual Development Cost Certificate for Project WA19-P054-016 and the Financial Statements for HUD Supported Programs are not a required part of the financial statements but are supplemental information required by HUD. Such information has been subjected to the auditing procedures applied in the audit of the financial statements and, in our opinion, is fairly presented in all material respects in relation to the financial statements taken as a whole.

In accordance with *Government Auditing Standards*, we have also issued a report dated July 12, 1996, on our consideration of the housing authority's internal control structure and a report dated July 12, 1996, on its compliance with laws and regulations.

Brian Sonntag
State Auditor

July 12, 1996

PIERCE COUNTY HOUSING AUTHORITY
Pierce County, Washington
July 1, 1994 Through June 30, 1995

Independent Auditor's Report On Supplementary Information
Schedule Of Federal Financial Assistance

Board of Commissioners
Pierce County Housing Authority
Tacoma, Washington

We have audited the general-purpose financial statements of the Pierce County Housing Authority, Pierce County, Washington, as of and for the fiscal year ended June 30, 1995, and have issued our report thereon dated July 12, 1996. Our report was modified because the housing authority was unable to provide written representations that generally accepted auditing standards require us to obtain and because the financial statements contain several departures from generally accepted accounting principles. These financial statements are the responsibility of the housing authority's management. Our responsibility is to express an opinion on these financial statements based on our audit.

As discussed in the following paragraph, we conducted our audit in accordance with generally accepted auditing standards and *Government Auditing Standards*, issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinion.

Because of the resignations of the housing authority's executive director, chief financial officer, and controller, we were unable to obtain written representations from the authority's management that generally accepted auditing standards require us to obtain.

Our audit was made for the purpose of forming an opinion on the financial statements of the Pierce County Housing Authority taken as a whole. The accompanying Schedule of Federal Financial Assistance is presented for purposes of additional analysis and is not a required part of the financial statements. The information in the schedule has been subjected to the auditing procedures applied in the audit of the financial statements and, in our opinion, is fairly presented in all material respects in relation to the financial statements taken as a whole.

Brian Sonntag
State Auditor

July 12, 1996

PIERCE COUNTY HOUSING AUTHORITY
Pierce County, Washington
July 1, 1994 Through June 30, 1995

**Independent Auditor's Report On Compliance With The General Requirements
Applicable To Federal Financial Assistance Programs**

Board of Commissioners
Pierce County Housing Authority
Tacoma, Washington

We have audited the general-purpose financial statements of the Pierce County Housing Authority, Pierce County, Washington, as of and for the fiscal year ended June 30, 1995, and have issued our report thereon dated July 12, 1996. Our report was modified because the housing authority was unable to provide written representations that generally accepted auditing standards require us to obtain and because the financial statements contain several departures from generally accepted accounting principles.

We have applied procedures to test the housing authority's compliance with the following requirements applicable to its federal financial assistance programs, which are identified in the Schedule of Federal Financial Assistance, for the fiscal year ended June 30, 1995:

- Political activity
- Davis-Bacon Act
- Civil rights
- Cash management
- Relocation assistance and real property acquisition
- Federal financial reports
- Allowable costs/cost principles
- Drug-Free Workplace Act
- Administrative requirements, including subrecipient monitoring

Except as described in the following paragraph, our procedures were limited to the applicable procedures described in the Office of Management and Budget's (OMB) *Compliance Supplement for Single Audits of State and Local Governments* or alternative procedures. Our procedures were substantially less in scope than an audit, the objective of which is the expression of an opinion on the housing authority's compliance with the requirements listed in the preceding paragraph. Accordingly, we do not express such an opinion.

Because of the resignations of the housing authority's executive director, chief financial officer, and controller, we were unable to obtain written representations from the authority's management that generally accepted auditing standards require us to obtain.

With respect to the items tested, the results of those procedures disclosed no material instances of noncompliance with the requirements listed in the second paragraph of this report. With respect to items not tested, nothing came to our attention that caused us to believe that the housing authority had

not complied, in all material respects, with those requirements. However, the results of our procedures disclosed an immaterial instance of noncompliance with those requirements, which is described in the accompanying Schedule of Federal Findings.

This report is intended for the information of management, officials of HUD, and the board of commissioners and to meet our statutory reporting obligations. This report is a matter of public record and its distribution is not limited. It also serves to disseminate information to the public as a reporting tool to help citizens assess government operations.

Brian Sonntag
State Auditor

July 12, 1996

PIERCE COUNTY HOUSING AUTHORITY
Pierce County, Washington
July 1, 1994 Through June 30, 1995

Independent Auditor's Report On Compliance With Specific Requirements
Applicable To Major Federal Financial Assistance Programs

Board of Commissioners
Pierce County Housing Authority
Tacoma, Washington

We have audited the general-purpose financial statements of the Pierce County Housing Authority, Pierce County, Washington, as of and for the fiscal year ended June 30, 1995, and have issued our report thereon dated July 12, 1996. Our report was modified because the housing authority was unable to provide written representations that generally accepted auditing standards require us to obtain and because the financial statements contain several departures from generally accepted accounting principles.

We also have audited the housing authority's compliance with the requirements applicable to its major federal financial assistance programs, which are identified in the accompanying Schedule of Federal Financial Assistance, for the fiscal year ended June 30, 1995. Those requirements are described in the HUD *Public and Indian Housing Compliance Supplement* (interim guidance, June 1995).

The management of the housing authority is responsible for the housing authority's compliance with those requirements. Our responsibility is to express an opinion on compliance with those requirements based on our audit.

Except as discussed in the following paragraph, we conducted our audit of compliance with those requirements in accordance with generally accepted auditing standards, *Government Auditing Standards*, issued by the Comptroller General of the United States, and OMB Circular A-128, *Audits of State and Local Governments*. Those standards and OMB Circular A-128 require that we plan and perform the audit to obtain reasonable assurance about whether material noncompliance with the requirements referred to above occurred. An audit includes examining, on a test basis, evidence about the housing authority's compliance with those requirements. We believe that our audit provides a reasonable basis for our opinion.

Because of the resignations of the housing authority's executive director, chief financial officer, and controller, we were unable to obtain written representations from the authority's management that generally accepted auditing standards require us to obtain.

The results of our audit procedures disclosed immaterial instances of noncompliance with the requirements referred to in the second paragraph, which are described in the accompanying Schedule of Federal Findings. We have considered the instances of noncompliance in forming our opinion on compliance, which is expressed in the following paragraph.

In our opinion, except for the effects of such adjustments, if any, as might have been determined to be necessary had we been able to obtain written representations from management, the Pierce County Housing Authority complied, in all material respects, with the requirements referred to in the second paragraph of this report that are applicable to its major federal financial assistance programs for the fiscal year ended June 30, 1995.

This report is intended for the information of management, officials of HUD, and the board of commissioners and to meet our statutory reporting obligations. This report is a matter of public record and its distribution is not limited. It also serves to disseminate information to the public as a reporting tool to help citizens assess government operations.

Brian Sonntag
State Auditor

July 12, 1996

PIERCE COUNTY HOUSING AUTHORITY
Pierce County, Washington
July 1, 1994 Through June 30, 1995

**Independent Auditor's Report On Internal Control Structure Used In
Administering Federal Financial Assistance Programs**

Board of Commissioners
Pierce County Housing Authority
Tacoma, Washington

We have audited the general-purpose financial statements of the Pierce County Housing Authority, Pierce County, Washington, as of and for the fiscal year ended June 30, 1995, and have issued our report thereon dated July 12, 1996. Our report was modified because the housing authority was unable to provide written representations that generally accepted auditing standards require us to obtain and because the financial statements contain several departures from generally accepted accounting principles. We have also audited their compliance with requirements applicable to major federal financial assistance programs and have issued our report thereon dated July 12, 1996.

Except as described in the following paragraph, we conducted our audit in accordance with generally accepted auditing standards, *Government Auditing Standards*, issued by the Comptroller General of the United States, and the provisions of OMB Circular A-128, *Audits of State and Local Governments*. Those standards and OMB Circular A-128 require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement and about whether the housing authority complied with laws and regulations, noncompliance with which would be material to a major federal financial assistance program.

Because of the resignations of the housing authority's executive director, chief financial officer, and controller, we were unable to obtain written representations from the authority's management that generally accepted auditing standards require us to obtain.

In planning and performing our audit, we considered the housing authority's internal control structure in order to determine our auditing procedures for the purpose of expressing our opinions on the financial statements and on compliance with requirements applicable to major federal assistance programs and to report on the internal control structure in accordance with OMB Circular A-128. This report addresses our consideration of internal control structure policies and procedures relevant to compliance with requirements applicable to federal financial assistance programs. We have addressed internal control structure policies and procedures relevant to our audit of the financial statements in a separate report dated July 12, 1996.

The management of the housing authority is responsible for establishing and maintaining an internal control structure. In fulfilling this responsibility, estimates and judgments by management are required to assess the expected benefits and related costs of internal control structure policies and procedures. The objectives of an internal control structure are to provide management with reasonable, but not absolute, assurance that:

- Assets are safeguarded against loss from unauthorized use or disposition.
- Transactions are executed in accordance with management's authorization and recorded properly to permit the preparation of financial statements in accordance with generally accepted accounting principles.
- Federal financial assistance programs are managed in compliance with applicable laws and regulations.

Because of inherent limitations in any internal control structure, errors, irregularities, or instances of noncompliance may nevertheless occur and not be detected. Also, projection of any evaluation of the structure to future periods is subject to the risk that procedures may become inadequate because of changes in conditions or that the effectiveness of the design and operation of policies and procedures may deteriorate.

For the purpose of this report, we have classified the significant internal control structure policies and procedures used in administering federal financial assistance programs in the following categories:

- **Accounting Controls**
 - Cash receipts
 - Cash disbursements
 - Receivables
 - Accounts payable
 - Purchasing and receiving
 - Payroll
 - Property, plant, and equipment
 - General ledger
- **General Requirements**
 - Political activity
 - Davis-Bacon Act
 - Civil rights
 - Cash management
 - Relocation assistance and real property acquisition
 - Federal financial reports
 - Allowable costs/cost principles
 - Drug-Free Workplace Act
 - Administrative requirements, including subrecipient monitoring
- **Specific Requirements as described in the HUD *Public and Indian Housing Compliance Supplement***

For all of the applicable internal control structure categories listed above, we obtained an understanding of the design of relevant policies and procedures and determined whether they have been placed in operation, and we assessed control risk.

During the fiscal year ended June 30, 1995, the housing authority expended 100 percent of its total federal financial assistance under major federal financial assistance programs.

We performed tests of controls, as required by OMB Circular A-128, to evaluate the effectiveness of the design and operation of internal control structure policies and procedures that we considered relevant to preventing or detecting material noncompliance with specific requirements, general requirements, and requirements governing claims for advances and reimbursements, and amounts claimed or used for matching that are applicable to the housing authority's major federal financial

assistance programs, which are identified in the accompanying Schedule of Federal Financial Assistance. Our procedures were less in scope than would be necessary to render an opinion on these internal control structure policies and procedures. Accordingly, we do not express such an opinion.

We noted certain matters involving the internal control structure and its operation that we consider to be reportable conditions under standards established by the American Institute of Certified Public Accountants. Reportable conditions involve matters coming to our attention relating to significant deficiencies in the design or operation of the internal control structure that, in our judgment, could adversely affect the housing authority's ability to administer federal financial assistance programs in accordance with applicable laws and regulations.

The matters involving the internal control structure and its operation that we consider to be reportable conditions are included in the Schedules of Findings and Federal Findings accompanying this report.

A material weakness is a reportable condition in which the design or operation of one or more of the specific internal control structure elements does not reduce to a relatively low level the risk that errors or irregularities in amounts that would be material in relation to the financial statements being audited may occur and not be detected within a timely period by employees in the normal course of performing their assigned functions.

Our consideration of the internal control structure policies and procedures used in administering federal financial assistance would not necessarily disclose all matters in the internal control structure that might be reportable conditions and, accordingly, would not necessarily disclose all reportable conditions that are considered to be material weaknesses as defined above. However, we noted a reportable condition involving the accounting internal control structure and its operation that we believe to be a material weakness as defined above. The condition, which is identified in the Schedule of Findings accompanying this report, was considered in determining the nature, timing, and extent of the procedures to be performed in our audit of the housing authority's compliance with requirements applicable to its major federal financial assistance programs for the fiscal year ended June 30, 1995, and this report does not affect our report thereon dated July 12, 1996.

This report is intended for the information of management, officials of HUD, and the board of commissioners and to meet our statutory reporting obligations. This report is a matter of public record and its distribution is not limited. It also serves to disseminate information to the public as a reporting tool to help citizens assess government operations.

Brian Sonntag
State Auditor

July 12, 1996

PIERCE COUNTY HOUSING AUTHORITY
Pierce County, Washington
July 1, 1994 Through June 30, 1995

Schedule Of Federal Findings

All Programs

1. Audit Reports Should Be Completed In Accordance With Federal Requirements

The fiscal year 1995 annual audit for Pierce County Housing Authority could not be completed in a timely manner as required by federal regulations.

The delay in completion of the audit was caused by the housing authority's lack of accurately prepared financial statements, poor internal controls and poor condition of the accounting records, as noted in the findings throughout this report.

OMB A-128, Section 13, Subpart f, states:

The reports shall be sent within 30 days after the completion of the audit, but no later than one year after the end of the audit period unless a longer period is agreed to with the cognizant audit agency.

The delay in reporting the audit results denies the federal government and other users timely information from which to make funding decisions and other pertinent decisions which stem from this report.

We recommend the housing authority implement corrective action to resolve the internal and accounting control problems noted in this report.

Auditee's Response

The Authority is taking corrective action to ensure that proper documentation and accounting procedures are followed in the future to ensure timely and accurate information.

CFDA 14.855 Section 8 Voucher and CFDA 14.857 Section 8 Certificate Programs

2. The Housing Authority Should Strengthen Internal Controls Over Section 8 Financial Information

Internal controls over the housing authority's accounting system were not adequate to ensure the accuracy of accounting information as it pertains to the Section 8 certificate and voucher programs. These weaknesses in the internal controls affected the housing authority's ability to prepare accurate year-end federal financial reports.

Upon further investigation, we found numerous mispostings related to the authority's attempt to transfer the Section 8 certificate and voucher programs' operating reserves to general operations to help pay debt service obligations of the authority's enterprise funds. One error compounded another. Because accounts were subsequently misstated, management continued on several occasions throughout fiscal 1995 to transfer nonexistent funds from the Section 8 reserves to general operations, sporadically creating more posting errors.

These errors were compounded by several internal audit adjustments made to the Section 8 certificate and voucher operating reserve accounts. We found no support for these adjustments.

At year-end, the housing authority's former controller prepared and submitted form HUD-52681 to HUD. However, due to the internal audit adjustments and posting errors stated above, the amounts reported from the housing authority's general ledger did not agree to HUD's internal records. HUD approved the form but revised several of the figures, including adjusting the voucher program operating reserve from the June 30, 1995 ending balance of \$33,448.63 to \$83,201.39 and the certificate operating reserve from \$131,099.57 to \$154,625.99.

The former controller then attempted to adjust the housing authority's operating reserve accounts to HUD's figures. However, because of the above mentioned internal audit adjustments and posting errors, the adjustments made by the former controller actually only compounded the earlier errors.

Per review of the detailed records and discussions with current housing authority accounting staff, the actual balances for both the Section 8 certificate and voucher programs should be zero as **all** surplus funds for fiscal year 1995 had been transferred to help service debt obligations. As a result of our audit, the housing authority finance department has already corrected these accounts and adjusted them to zero, accordingly.

These errors resulted from inadequate internal controls. There was a lack of supervision, authorization, documentation and training. The former controller was responsible for Section 8 financial information and reporting. None of the controller's journal entries were reviewed by the former chief financial officer or any other person in the finance department. Further, the housing authority's interfund transactions are quite complicated given the computerized accounting system utilized by the housing authority. The accounting system automatically "creates" an interfund data entry if one is not booked; the former controller may not have completely understood the process.

Lack of controls increases the risk that errors or irregularities could go undetected for some time and impairs the ability to prepare accurate and timely financial information.

We recommend housing authority officials develop adequate internal controls whereby:

- a. All journal entries are reviewed and approved
- b. Supporting documentation is prepared and retained for all adjustments
- c. Personnel are fully trained in utilizing the computerized accounting system.

We further recommend an employee in the finance department review and reconcile the general ledger accounts to the amounts as reported by HUD.

Auditee's Response

The Authority is taking corrective action to ensure that proper documentation and accounting procedures are followed in the future to ensure timely and accurate information.

3. The Housing Authority Should Calculate, Record, And Report Section 8 Administrative Fees Utilizing The HUD Approved Methodology

The housing authority earns administrative fees for managing the Section 8 certificate and voucher programs. The fees are calculated by using HUD prescribed guidelines and are reported on a supplemental schedule to form HUD-52681, 'Voucher for Payment of Annual Contributions and Operating Statement.' The amounts calculated and reported as earned on the administrative fee supplemental schedule for nine months of fiscal year 1995 did not agree with the housing authority's general ledger.

The housing authority's accountant computed all of fiscal year 1995's administrative fees earned under the blended rate method. He did so by posting fees for 1995 at the beginning of the year and adjusting out the differences between recorded and actual fees earned. When the accountant resigned, the housing authority's then controller took over the calculation of the administrative fee and realized there was a discrepancy. The housing authority had earned substantially more than had been claimed (\$10,839.54 in certificates and \$29,020.17 in vouchers) and billed HUD for the difference, which HUD paid.

Upon receipt, the amounts were incorrectly recorded in the housing authority's general ledger, resulting in overstated Section 8 and understated general operations revenues. Current personnel in the finance department have subsequently corrected these errors.

These errors can be attributed to inadequate internal controls. There was a lack of oversight or review of the former accountant's work and the former controller's journal entries which misposted the additional administrative fees earned. In addition, the former accountant was allowed to prepost a year's worth of journal entries and then 'adjust out' differences.

Lack of controls increases the risk that errors or irregularities could go undetected for some time. The misposting of the additional fees earned remained undetected until our audit.

We recommend housing authority officials develop adequate internal controls including proper oversight and review, and the posting of transactions as they occur.

Auditee's Response

As per the Draft Audit Report, corrective action has already taken place.

4. The Housing Authority Should File Federal Forms In A Timely Manner

Section 8 certificate and voucher forms required to be submitted to HUD were filed late.

HUD Handbook 7420.7, Chg-4, step 12.5 states:

The PHA must submit form HUD-52672, 'Supporting Data For Annual Contributions Estimates' and form HUD-52673, 'Estimate of Total Required Annual Contributions' to the field office for approval . . . The forms must be submitted at least 90 calendar days before the beginning of each PHA fiscal year.

As the housing authority's fiscal year began on July 1, 1994, form HUD-52672 and HUD-52673 were required to be submitted 90 calendar days prior to that date, on April 1, 1994. For both the Section 8 certificate and voucher programs, the forms were filed on May 6, 1994. Thus, the housing authority was not in compliance with the required filing deadlines for those reports.

No members of management responsible for the filing of these reports remain employed by the housing authority; current finance staff do not know why these forms were filed after the required deadline.

Failure to file federal financial reports within the deadline potentially jeopardizes the housing authority's ability to continue to receive federal funds.

We recommend housing authority officials implement controls to ensure all required federal financial reports are filed within the applicable deadlines.

Auditee's Response

The Authority is taking corrective action to ensure that proper documentation and accounting procedures are followed in the future to ensure timely and accurate information.

CFDA 14.850 Public Housing Program

5. The Public Housing Management Assessment Program (PHMAP) Certification Submitted To HUD Should Be Reviewed By Management

The PHMAP certificate is used by HUD to assess the management performance and capabilities of the housing authority in managing low-income housing. The PHMAP report submitted to HUD for fiscal year 1995 contained the following errors:

- a. The 'average number of days to bring non-emergency maintenance items to Housing Quality Standards' was 17 rather than the 4 days reported.
- b. The 'average number of days to correct identified systems deficiencies' was 23 rather than the 2 days reported.

PIH 95-31, *Interim Guidance for Annual Audits of Public Housing Agencies and Indian Housing Agencies by Independent Auditors* Chapter 5, Section 5-2, states in part:

The PHMAP assessment is performed by field offices on an annual basis. The PHA is required to certify to several of the indicators after the end of each fiscal year, and is required to maintain supporting documentation for post-review purposes. As a result of the PHMAP assessment, the PHA is rated as either high-performing, standard or troubled and/or mod-troubled.

These errors were the result of inadvertently using the prior year data and could have been prevented with proper review.

Per HUD, neither of the above errors had an effect on the housing authority's PHMAP score or performer status. However, such errors could potentially mislead HUD in rating the housing authority's performance and, as a result, HUD may inappropriately reduce requirements such as the submission of an indirect cost allocation plan.

We recommend housing authority officials develop and implement controls, including review, to ensure figures as presented on the PHMAP are accurate and supported by underlying records.

Auditee's Response

The Authority has provided the proper training and over sight to the responsible employees in the submission of the certifications.

CFDA 14.850 Public Housing, CFDA 14.855 Section 8 Voucher, and CFDA 14.857 Section 8 Certificate Programs

6. The Housing Authority Should Adhere To Compliance Requirements Pertaining To The Family Self Sufficiency Program

If the earned income of a family participating in the Family Self Sufficiency (FSS) program increases, the housing authority must establish an `escrow account' for the family and credit to this account a portion of the increase in rent that would otherwise result from the increases in earned income.

One family participated in the housing authority's (FSS) program during fiscal year 1995. The family entered the program December 1994 and withdrew February 1995 with a total escrow of \$534. The escrow account was not established by the housing authority until November 1995, nearly eleven months later. Neither general nor subsidiary ledgers for the FSS program were established until October 1995.

HUD interim Public and Indian Housing (PIH) Compliance Supplement, PIH 95-31, *Interim Guidance for Annual Audits of Public Housing Agencies and Indian Housing Authorities by Independent Auditors*, Chapter 7, requires the auditor to:

Determine that the general ledger combined FSS investment account is supported by a subsidiary ledger showing each family's FSS escrow balance

Determine that the FSS funds are deposited into a HUD approved investment.

The finance staff responsible for the FSS program during fiscal year 1995 are no longer employed by the housing authority. Current staff do not know why the employees responsible for depositing these funds failed to do so, or why general and subsidiary ledgers were not established at the time the family became active in the FSS program.

We recommend the housing authority make timely deposit of FSS funds in a HUD-approved investment account and maintain appropriate general and subsidiary ledgers.

Auditee's Response

The Authority has taken corrective action in this area and has created the appropriate ledger entries to account for the FSS Funds.

Auditor's Concluding Remarks

Based upon the response, the issues delineated in our report appear to have been addressed. We will review these areas again in our subsequent audit.

We would like to express our appreciation to staff for their assistance and cooperation throughout the audit process.

PIERCE COUNTY HOUSING AUTHORITY
Pierce County, Washington
July 1, 1994 Through June 30, 1995

Status Of Prior Findings

The findings contained in the prior audit report was resolved as follows:

1. General Ledger Internal Controls Should Be Improved

Resolution: *Finding is repeated.*